

## Granny Flats

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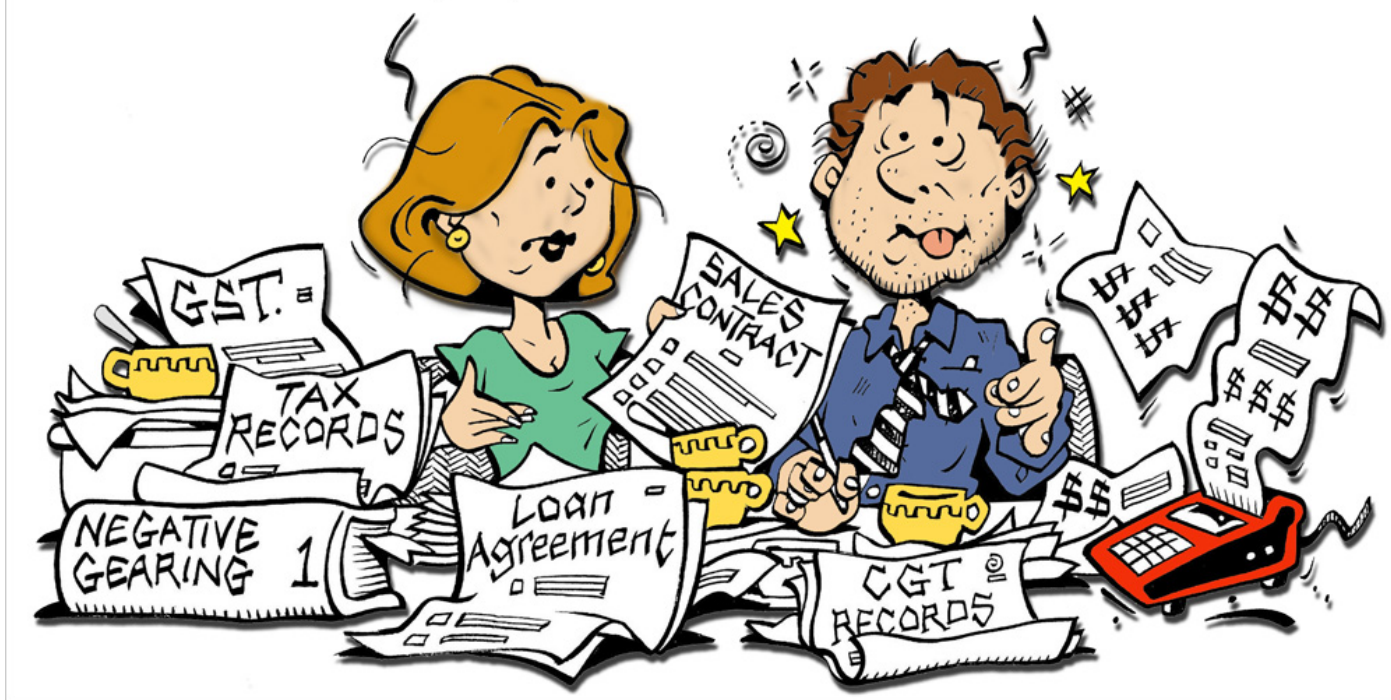
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Darl, an Accountant would explain all this in a jiffy...

OMG, that's a tax-deductible jiffy. too.



## Granny Flat Tax Issues

Important points to discuss with your Accountant before you build a Granny Flat in your back yard.

- 1) If you are building the Granny Flat to rent out and it is in the back yard of your home then this is very similar to renting out rooms in your house which is covered by ATO ruling IT 2167 <https://www.ato.gov.au/law/view/document?DocID=ITR/IT2167/NAT/ATO/00001> . If up until that point in time it has only been used as your home then section 118-192 ITAA 1997 will reset your cost base to market value at the date it first earns income. From that point onwards only the portion of the property that you use as your home will be protected from CGT by your main residence exemption.
- 2) If you are building the Granny Flat to house a family member then as long as both households interact frequently and it is not earning income both units could be considered one dwelling for capital gains tax purposes and both buildings will be covered by the main residence exemption. Reference TD 1999/69 <https://www.ato.gov.au/law/view/document?locid=txd/td199969/nat/ato>
- 3) Centrelink permits pensioners to sell their home and pay money to their child for a right to occupy part of the child's home, without triggering the gifting provisions. They also strongly recommend that a legal right to occupy is put in place to protect against elder abuse. Careful here, if this legal right is not done properly it will trigger a CGT event for the child on the full amount, no 50% CGT discount and no main residence exemption. The full amount is the market value of the equivalent rent over the parent's life expectancy even if no money changes hands.

From 1<sup>st</sup> July 2021 the government has introduced an exception from this CGT rip off but there are a few catches to trap the unwary such as it can only apply if the parent has reached age pension age, the property must be owned by an individual (not a SMSF, company or trust) and they must not pay rent. If you can't meet these conditions it maybe more practical for the parent to actually buy part of the property so the transaction can be covered by the main residence exemption. There is much more information about providing a granny flat for your parent in this blog <https://bantacs.com.au/Jblog/granny-flat-rights/#more-262>

- 4) If you build a Granny Flat on a property that you purchased before 20<sup>th</sup> September, 1985 then you have created an asset that is separate from the land and your house. The land and original building are still considered a pre CGT asset but the Granny Flat will be a post CGT asset and subject to CGT unless covered by your main residence exemption as discussed above.
- 5) If you think you will be caught with some CGT, when you eventually sell the property, then make the most of section 110-25(4) ITAA 1997. This section allows you to increase your cost base by the costs of holding the whole property, such as rates, insurance, interest, cleaning materials, lawn mower fuel, light globes, just keep lots of records. These expenses cannot have otherwise been claimed as a tax deduction (ie against the rent received) and cannot be used to create a capital loss.

Now the way the CGT formula works is you work out the capital gain on the whole property first, then apportion it on the ratio of the percentage of the area covered by your main residence exemption and the percentage of the area not covered. This flat pro rata apportionment based only on a percentage does not take into account, when calculating the capital gain, whether the expenses relate to the side covered by your main residence exemption or not. Effectively allowing a portion of the costs associated with the exempt side to reduce the capital gain on the side that is exposed to CGT. Meanwhile the expenses relating to the side exposed to CGT have already been claimed as a tax deduction. The best tax tip is to keep good receipts.

### **How To Get Your Questions Answered:**

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Disclaimer: Please note that by the time you read this information it may be out of date. The information is presented in summary form and intended only to draw your attention to issues you should further discuss with your accountant. Do not act on this information without further advice as to your particular circumstances.

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